House of Commons

Committee of Public Accounts

Department for Transport: The InterCity East Coast Passenger Rail Franchise

Thirty-ninth Report of Session 2010–12

Report, together with formal minutes, oral and written evidence

Ordered by the House of Commons to be printed 22 June 2011

HC 1035
Published on 9 July 2011
by authority of the House of Commons
London: The Stationery Office Limited
£8.50

Committee of Public Accounts

The Committee of Public Accounts is appointed by the House of Commons to examine "the accounts showing the appropriation of the sums granted by Parliament to meet the public expenditure, and of such other accounts laid before Parliament as the committee may think fit" (Standing Order No 148).

Current membership

Rt Hon Margaret Hodge (*Labour, Barking*) (Chair)
Mr Richard Bacon (*Conservative, South Norfolk*)
Mr Stephen Barclay (*Conservative, North East Cambridgeshire*)
Dr Stella Creasy (*Labour/Cooperative, Walthamstow)*
Jackie Doyle-Price (*Conservative, Thurrock*)
Justine Greening (*Conservative, Putney*)
Matthew Hancock (*Conservative, West Suffolk*)
Chris Heaton-Harris (*Conservative, Daventry*)
Joseph Johnson (*Conservative, Orpington*)
Rt Hon Mrs Anne McGuire (*Labour, Stirling*)
Mr Austin Mitchell (*Labour, Great Grimsby*)
Nick Smith (*Labour, Blaenau Gwent*)
Ian Swales (*Liberal Democrats, Redcar*)
James Wharton (*Conservative, Stockton South*)

The following member was also a member of the committee during the parliament:
Eric Joyce (*Labour, Falkirk*)

Powers

The committee is one of the departmental select committees, the powers of which are set out in House of Commons Standing Orders, principally in SO No 152. These are available on the internet via www.parliament.uk.

Publication

The Reports and evidence of the Committee are published by The Stationery Office by Order of the House. All publications of the Committee (including press notices) are on the internet at www.parliament.uk/pac. A list of Reports of the Committee in the present Parliament is at the back of this volume.

Additional written evidence may be published on the internet only.

Committee staff

The current staff of the Committee is Philip Aylett (Clerk), Lori Verwaerde (Senior Committee Assistant), Ian Blair and Michelle Garratty (Committee Assistants) and Alex Paterson (Media Officer).

Contacts

All correspondence should be addressed to the Clerk, Committee of Public Accounts, House of Commons, 7 Millbank, London SW1P 3JA. The telephone number for general enquiries is 020 7219 5708; the Committee's email address is pubaccom@parliament.uk.

Contents

Summary

Since the mid 1990s, passenger rail services have been delivered through a system of franchises. Each franchise is a competitively procured contract, typically lasting seven to ten years, between the Department for Transport and a private train operating company. Companies bid for franchises on the basis of the amount of subsidy they require, or the premium they would be prepared to pay, to run services on a defined part of the rail network. Bids include each company's forecast of what revenue they can expect, based on assumptions about the number and type of passenger journeys and the prices they can charge.

The InterCity East Coast Mainline is a hugely significant rail service, carrying around 19 million passengers a year between London, the North East and Scotland. The franchise has had a troubled history. In 2005, a contract was awarded to Great North Eastern Railway, but financial difficulties at its holding company meant that the franchise failed 18 months later.

In 2007, a new contract was awarded to National Express to run the franchise on the basis that it would pay the Department £1.4 billion over seven and a half years. At the time, the East Coast franchise was one of three operated by National Express, which also ran passenger services in the South East and East Anglia. As a result of the economic downturn, expected passenger revenues did not materialise and National Express announced in July 2009 that it wanted to opt out of the contract and would not provide the necessary financial support to the East Coast franchise.

Following negotiations with National Express, the Department terminated the contract in November 2009 and transferred services to a new publicly owned company, Directly Operated Railways, until the franchise could be re-tendered. Although other franchises suffered financial difficulties during the economic downturn, East Coast was the only franchise that failed.

In negotiations, the Department turned down an offer worth £150 million from National Express to exit the franchise by mutual consent. Instead the Department chose to terminate the contract, and received £120 million from National Express. The Department judged that foregoing the extra cash would reduce the risk of other train operating companies with loss-making franchises seeking similar deals, but the taxpayer did forfeit £30 million. The Department allowed National Express to keep its two other franchises, and in December 2010 told National Express that the termination would not be held against the company if it bid for future franchises.

Since the East Coast termination, other franchises have been in financial difficulty and their holding companies have not sought to hand them back. We are, however, concerned that the Department created a moral hazard by allowing National Express to pay a lesser financial penalty through terminating a contract than it would have done by paying £150 million to exit consensually, and by choosing not to hold the termination against National Express in future bids.

The Department has potentially incentivised other holding companies with loss-making

franchises to terminate, rather than renegotiate, their contract with the Department, as they know doing so will cost them less and will not affect their ability to compete for other contracts.

On the basis of a report from the Comptroller and Auditor General[1] we took evidence from the Department and Directly Operated Railways on protecting the taxpayer, performance of the franchise in public ownership and the lessons to be learnt.

1 C&AG's Report, *Department for Transport: The InterCity East Coast Passenger Rail Franchise*, Session 2010-11, HC 824

Conclusions and recommendations

1. **The Department did not undertake sufficient due diligence on the bid by National Express for the East Coast franchise.** National Express promised the largest ever payment for a passenger rail franchise, but then failed to meet its profit forecasts from the start of the contract and, following the economic downturn, quickly started to accumulate losses. Crucially, the Department did not test any of the bids for the franchise against the impact of an economic downturn. The Department should always test bids in future against different economic conditions. This becomes more important with the move to much longer franchises of up to 22 years. The Department should improve its arrangements with franchisees to remove any incentive on bidders to make forecasts which are either too optimistic, thereby increasing the risk that the franchise might fail, or deliberately pessimistic, thereby increasing their expected profits. For instance, the Department should have been more rigorous in questioning National Express on its assessment that it could grow passenger revenue by 5%-12% per annum. By any measure, this appears to be an over-optimistic assessment of the business.

2. **In public ownership, the franchise is now performing better than expected but the Department has still foregone some £330 million - £380 million of expected revenue.** Unlike other train operators, which continued to bear losses during the economic downturn, National Express did not have the resources or the inclination to fulfil the terms of its contract. The holding company had accumulated more than £1 billion in debt and needed to refinance this debt following the downturn. Part of the company's solution to this was to avoid heavy forecast losses on the East Coast franchise by negotiating with the Department to leave the contract. The Department should in future take greater care when assessing the financial strength of a company to ensure it will be able to support any of its franchises that get into financial difficulty. Specifically, the Department should avoid letting franchises to heavily indebted holding companies.

3. **The Department entered into negotiations demanding the surrender of National Express's other two franchises when they could not legally demand they do so.** After National Express sought changes to the terms of the contract, the Department offered a deal requiring a payment of £200 million and the surrender of the company's other two franchises. However, legal advice indicated that the Department did not have a right to terminate the company's other two franchises and so ended up leaving them in place. Contracts should give the Department a clear right to terminate a holding company's other franchises.

4. **National Express paid £120 million to get out of a contractual obligation to pay the taxpayer £1.4 billion.** The penalty National Express paid to the Department amounted to less than 9% of contract value, which leads one to question whether the taxpayer has been adequately compensated. This compensation is further reduced by the extension granted to the other two franchises and the additional revenue support given by the Department. The Department should ensure that there are stronger financial penalties in contracts for failure to meet contractual obligations.

5. **The Department turned down an offer from National Express of an extra £30 million for a "no fault" exit.** It judged that accepting such an offer would have increased the risk of other franchises seeking a similar settlement, costing the Department and the taxpayer £140-£280 million in the long run, according to the NAO. The Department wanted the reputational damage for National Express, of having one of its franchises terminated, to act as a clear warning signal to others. But the Department undermined that position by telling National Express just over a year after the termination that the failure would not be held against the company if it bid for future franchises. Since the East Coast termination, other franchises have been in financial difficulty, and the holding companies have not sought to hand them back. However, the Department has potentially incentivised other holding companies with loss-making franchises to terminate, rather than renegotiate, their contract with the Department, as they know doing so will cost them less and will not affect their ability to compete for other contracts. The Department should make it clear to holding companies that failure to deliver obligations will have serious lasting implications.

6. **Following a period of deterioration, punctuality on the line is now beginning to improve and investments are being made in new technology, fleet maintenance and customer service.** The unfortunate recent history of the franchise may well have caused under-investment in a service described to us as the "jewel in the railway crown". The investment of taxpayers' money while the franchise has been in public ownership should help to secure a good deal when it is retendered to the private sector in 2012. We expect the Department to ensure that this investment is fully recovered.

7. **Forecasts of future passenger revenues across the rail network have frequently proved inaccurate.** The high proportion of discretionary business and leisure travel on the East Coast line offers commercial opportunities to attract new passengers but makes revenues susceptible to changes in the economy. Forecasting is not straightforward as it depends on assumptions about the number and types of future journeys as well as the prices charged. However, such complications are hardly new and we have in the past highlighted the poor quality of data on passenger journeys. As more sophisticated data on passenger journeys becomes available, the Department should validate the assumptions that lie behind passenger revenue forecasts for each franchise. These should feed this into its wider budgeting for the amount of support that may be required from the taxpayer.

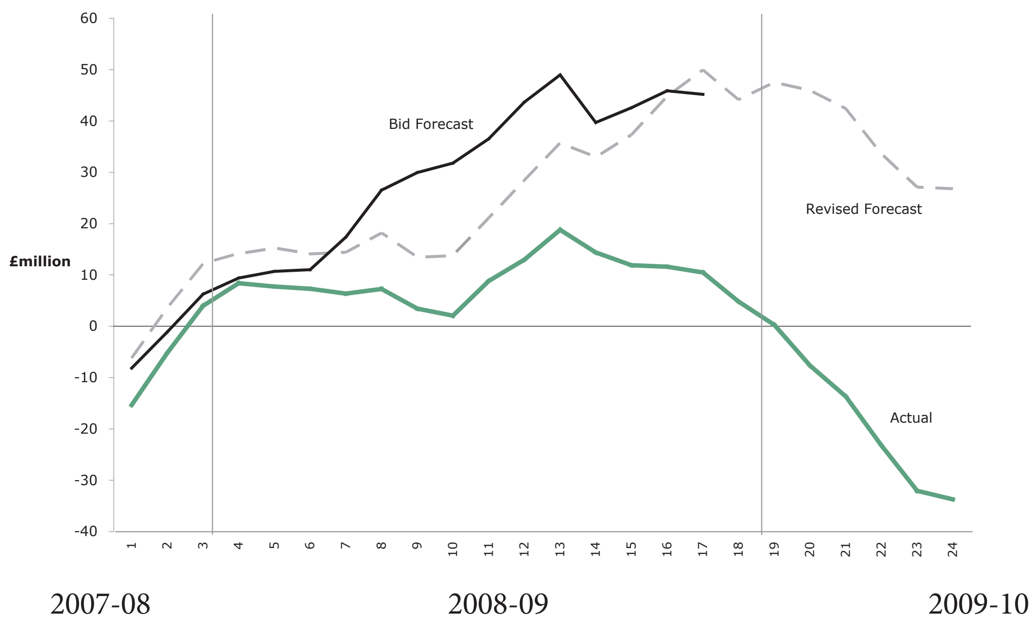
1 Protecting the taxpayer

1. National Express agreed in 2007 to pay the Department £1.4 billion over the seven and a half year contract to run the East Coast Mainline, the largest ever payment for a passenger rail franchise, on the basis of annual growth in passenger revenue of 5% -12%. But falling revenues as a result of the economic downturn put substantial pressure on the franchise and, after April 2009, cumulative profits quickly became cumulative losses.[2]

2. In its bid, National Express had included planned measures to cut costs and generate new business during the first year of the franchise. These plans were tested by the Department for deliverability. Taking into account the reliance of the franchise on discretionary business and leisure travel, rather than commuter journeys, and favourable forecasts for future growth in the economy, the Department judged that the National Express bid would be profitable and deliverable.[3] Nevertheless, the company failed to meet its financial targets from very early on (Figure 1).[4]

3. The Department should have been more rigorous in questioning National Express on its assessment that they could grow passenger revenue by 5%-12% per annum. By any measure, this appears to be an over-optimistic assessment of the business.

Figure 1: East Coast franchise cumulative profit and loss December 2007 to October 2009



2 C&AG's Report, paras 4, 1.17 and 2.6

3 Qq 1, 72

4 Q3

When bids for the franchise were being considered, neither the Department nor the company appears to have considered the prospect of an economic downturn. During the downturn which then materialised, other franchises dependent on discretionary travel suffered, but their holding companies did not request additional public support. National Express, however, had accumulated more than £1 billion in debt to expand its business and needed to refinance this debt in uncertain market conditions.[5] Part of the solution for the company was to avoid heavy forecast losses on the East Coast franchise by negotiating with the Department to leave the contract. The Department now accepts that, in future, it should test the impact on bids of a downturn in the economy and take a closer interest in the overall financial position of bidders' and franchisees' holding companies.[6]

4. The failure of the franchise led to a shortfall in expected income for the Department estimated to be £330 million – £380 million to the end of 2012.[7] However, following public ownership in November 2009, the franchise has recorded better than expected profits and, for 2011-12, expects to make around two-thirds of the payments to the Department that had been forecast by National Express in its original bid.[8]

5. In undertaking stress testing on future franchises for an economic downturn, the Department considers that there is a balance to be struck between mitigating against what would be an unlikely event and encouraging bidders to use their commercial judgement in putting forward proposals to increase passenger revenues.[9] Arrangements to support franchises where passenger revenues fail to meet expectations are being reviewed by the Department.[10] The difficulty with such arrangements is that although no taxpayer support would be provided to franchisees for the first four years, support is automatically payable thereafter. Such a lifeline from the taxpayer risks reducing the incentive for franchisees to work to increase passenger revenues.[11]

6. Under the terms of the contract, the termination of the East Coast franchise cost National Express nearly £120 million.[12] During the two years that the company ran the franchise, it paid the Department £235 million out of the promised £1.4 billion. The reason for terminating the contract rather than agreeing a consensual exit was that the Department did not consider that a holding company should be able to hand back a loss-making franchise, while keeping others that were profitable.[13] National Express's other franchises did make a profit - the profits on C2C were around £4 million in 2010-11 and on East Anglia around £15 million. The East Anglian franchise also received £37 million in revenue support from the taxpayer during 2010-11.[14]

5 Qq 3, 7

6 Qq 6-8; C&AG's Report, para 2.9

7 Q111

8 Qq 20-22; C&AG's Report, para 17

9 Q3

10 Q71

11 Q63

12 Q44

13 Qq 54-56, 59; C&AG's Report, para 2.35

14 Qq 56, 58, 70: Ev 13

7. Before terminating the East Coast contract, the Department sought the return of all three franchises run by National Express on a consensual basis. Based on a range of advice, the Department also considered whether all three franchises could be terminated, but it was advised that there was no clear event of default in the other two franchises.[15] Clearly the government should in future consider this issue in the letting of franchises. Companies should not be able to walk away from less profitable franchises but retain control of more profitable franchises.

8. In terminating the contract, the Department wanted to send a strong message that it placed greater weight on holding companies' supporting their loss-making franchisees, thereby preserving their reputations, than on payments for a consensual exit. However, National Express had offered £150 million for a consensual exit, some £30 million more than it ended up paying on contract termination.[16]

9. The Department tried to balance the direct costs of terminating the franchise with the potential cost of other franchises seeking to negotiate exits from loss-making franchises on similar terms. At the time, as many as five other franchises were in financial difficulty. Renegotiating the contract with National Express and the contracts of the five other franchises might have cost £420 million. The cost of terminating the East Coast franchise came to about £250 million, making it, in the Department's view, the more cost-effective option.

10. The Department told us that allowing National Express a consensual exit would have been better for the company's reputation and general market performance.[17] The Department was very clear in its view that there would be real moral hazard if it was seen not to be penalising failure. However, in December 2010, the Department informed National Express that the failure of the franchise would not be held against the company if it bid for future franchises -National Express had continued to run the East Anglia and C2C franchises profitably.[18] he Department said that it could not rule the company out of bidding for future franchises but had made no promises that it would automatically pre-qualify. In judging bids for future franchises, the Department has to be satisfied that bids would be deliverable and would in future place more importance on past performance. [19]

15 Qq 48, 51, 52, 60; C&AG's Report, para 2.19

16 Qq 39, 41-43; C&AG's Report, paras 2.21 and 2.24

17 Q59

18 Q29

19 Qq 32, 37; C&AG's Report, para 2.33

2 Performance since taking the franchise into public ownership

11. Punctuality on the East Coast line worsened since handover of the franchise to Directly Operated Railways, continuing a year-on-year downward trend. Most of the delays were attributable to Network Rail and other train operating companies that run trains on parts of the line, with 25% of the delay attributable to the East Coast franchise itself.[20]

12. The predominant cause of delays was an ageing train fleet that, over the years, had not been adequately maintained. In the last 18 months, Directly Operated Railways has been attempting to turn things around. By the end of 2010-11 the line recorded the lowest level of delay in the past 11 years; and the proportion of delay attributable to the East Coast franchise while in public ownership had now fallen to 21%. Directly Operated Railways told us that Network Rail recognises the need for further improvements to the infrastructure on the East Coast line and that it should be a top priority for its management.[21]

13. The witnesses described the East Coast Main Line as the “jewel in the railway crown”.[22] Directly Operated Railways informed the Committee that it is improving revenue-forecasting technology, investing in the train fleet and customer services to improve punctuality and generate extra revenue.[23] Much of the investment will benefit the franchise over the next four or five years and Directly Operated Railways expects that the taxpayer will see a return when the franchise is re-let in about 18 months time.[24] Directly Operated Railways is working to this timescale and told us that the Department is keen to understand the issues faced by previous franchisees ahead of preparing the invitation to tender for the new franchise.[25]

14. Directly Operated Railways told us that, on the East Coast franchise, discretionary business and leisure travellers account for some 96% of passenger revenues. Without a large and relatively stable revenue stream from commuters, forecasting passenger revenues for the franchise in an economic downturn is therefore particularly difficult.[26]

15. The Department considered that it was getting better at forecasting and was addressing the Committee’s past concerns about the collection of adequate data on passenger journeys, a pre-requisite for good demand forecasting. The Department told us it that it has always expected and allowed for shortfalls in revenue from rail franchises. In 2009-10, the actual amount of revenue support provided by the department had been £87 million higher than forecast. In the following year, however, the amount spent on revenue support

20 Qq 103, 104; C&AG’s Report, paras 3.8-3.9

21 Qq 75, 104

22 Q26

23 Q119

24 Q96

25 Q26

26 Q12

was £208 million lower than forecast and the Department had spent the unused funds on investments in the railways such as stations and the Manchester line.[27]

16. The Department told us it wants to develop more sophisticated contracts that put an emphasis on the train operator attracting passengers to trains that had spare capacity and away from services operating at full capacity.[28] The Department is therefore looking to give commercial operators more freedom to manage franchises in a way that more closely matches supply with demand.[29]

27 Qq 106-117; Ev 13

28 Q106

29 Q105

Formal Minutes

Wednesday 22 June 2011

Rt Hon Margaret Hodge, in the Chair

Mr Richard Bacon	Mrs Anne McGuire
Mr Stephen Barclay	Austin Mitchell
Dr. Stella Creasy	Nick Smith
Chris Heaton-Harris	Ian Swales
Jo Johnson	James Wharton

Draft Report (*Department for Transport: The InterCity East Coast Passenger Rail Franchise)* proposed by the Chair, brought up and read.

Ordered, That the draft Report be read a second time, paragraph by paragraph.

Paragraphs 1 to 16 read and agreed to.

Conclusions and recommendations 1 to 7 read and agreed to.

Summary read and agreed to.

Resolved, That the Report be the Thirty-ninth Report of the Committee to the House.

Ordered, That the Chair make the Report to the House.

Ordered, That embargoed copies of the Report be made available, in accordance with the provisions of Standing Order No. 134.

Written evidence was ordered to be reported to the House for placing in the Library and Parliamentary Archives.

[Adjourned till Monday 27 June at 3.30pm

Witnesses

List of printed written evidence

List of Reports from the Committee during the current Parliament

The reference number of the Government's response to each Report is printed in brackets after the HC printing number.

Session 2010–12

First Report	Support to incapacity benefits claimants through Pathways to Work	HC 404
Second Report	Delivering Mulit-Role Tanker Aircraft Capability	HC 425
Third Report	Tackling inequalities in life expectancy in areas with the worst health and deprivation	HC 470
Fourth Report	Progress with VFM savings and lessons for cost reduction programmes	HC 440
Fifth Report	Increasing Passenger Rail Capacity	HC 471
Sixth Report	Cafcass's response to increased demand for its services	HC 439
Seventh Report	Funding the development of renewable energy technologies	HC 538
Eighth Report	Customer First Programme: Delivery of Student Finance	HC 424
Ninth Report	Financing PFI projects in the credit crisis and the Treasury's response	HC 553
Tenth Report	Managing the defence budget and estate	HC 503
Eleventh Report	Community Care Grant	HC 573
Twelfth Report	Central government's use of consultants and interims	HC 610
Thirteenth Report	Department for International Development's bilateral support to primary education	HC 594
Fourteenth Report	PFI in Housing and Hospitals	HC 631
Fifteenth Report	Educating the next generation of scientists	HC 632
Sixteenth Report	Ministry of Justice Financial Management	HC 574
Seventeenth Report	The Academies Programme	HC 552
Eighteenth Report	HM Revenue and Customs' 2009-10 Accounts	HC 502
Nineteenth Report	M25 Private Finance Contract	HC 651
Twentieth Report	Ofcom: the effectiveness of converged regulation	HC 688
Twenty-First Report	The youth justice system in England and Wales: reducing offending by young people	HC 721
Twenty-second Report	Excess Votes 2009-10	HC 801
Twenty-third Report	The Major Projects Report 2010	HC 687

Twenty-fourth Report	Delivering the Cancer Reform Strategy	HC 667
Twenty-fifth Report	Reducing errors in the benefit system	HC 668
Twenty-sixth Report	Management of NHS hospital productivity	HC 741
Twenty-seventh Report	HM Revenue and Customs: Managing civil tax investigations	HC 765
Twenty-eighth Report	Accountability for Public Money	HC 740
Twenty-ninth Report	The BBC's management of its Digital Media Initiative	HC 808
Thirtieth Report	Management of the Typhoon project	HC 860
Thirty-first Report	HM Treasury: The Asset Protection Scheme	HC 785
Thirty-second Report	Maintaining financial stability of UK banks: update on the support schemes	HC 973
Thirty-third Report	National Health Service Landscape Review	HC 764
Thirty-fourth Report	Immigration: the Points Based System – Work Routes	HC 913
Thirty-fifth Report	The procurement of consumables by National Health Service acute and Foundation Trusts	HC 875
Thirty-seventh Report	Departmental Business Planning	HC 650
Thirty-eighth Report	The impact of the 2007-08 changes to public service pensions	HC 833
Thirty-ninth Report	Department for Transport: The InterCity East Coast Passenger Rail Franchise	HC 1035
Fortieth Report	Information and Communications Technology in government	HC 1050

Oral evidence

Taken before the Committee of Public Accounts

on Monday 9 May 2011

Members present:

Margaret Hodge (Chair)

Stephen Barclay
Stella Creasy
Matthew Hancock
Joseph Johnson
Mrs Anne McGuire
Austin Mitchell
James Wharton

Amyas Morse, Comptroller and Auditor General, and Geraldine Barker, Director, NAO, gave evidence. **Gabrielle Cohen**, Assistant Auditor General, NAO, and **Marius Gallaher**, Alternate Treasury Officer of Accounts, HM Treasury, were in attendance.

REPORT BY THE COMPTROLLER AND AUDITOR GENERAL

The InterCity East Coast Passenger Rail Franchise (HC 824)

Examination of Witnesses

Witnesses: **Lin Homer**, Permanent Secretary, Department for Transport, and **Elaine Holt**, Chief Executive, Directly Operated Railways Ltd, Chairman, East Coast Main Line Company Ltd, gave evidence.

Q1 Chair: Welcome for the first time to Lin Homer in her new job, so congratulations on becoming a Permanent Secretary. That is the good news. The bad news is that, on Wednesday, we are looking at the regulator and, as I reflected on that, I thought it was important that we should have the Department's view on that. Whilst we are going to be kind to you and not give you two in a week, we will want you to come and give us further evidence on the Department's view of the regulator as soon as we can fit that into our programme, but welcome—we look forward to some good hearings. Elaine Holt, it is certainly your first time in front of the new Committee—you have probably been up before—so welcome as well.

I am going to start, if I can, with you, Lin, around the original franchise to National Express, because the original franchise was for £1.4 billion and, as we read the Report, we see that the Department, during that time, thought the franchise could be worth anything between about £900 million and £1.5 billion, and you settled at this £1.4 billion figure. Were you too greedy?

Lin Homer: I do not think, Chairman, that we were too greedy. I think it is always a question of testing the commercial view, and that is part of the reason why we let franchises. I have had a very thorough look at the assessments that were made and the judgments that were made, and I think, taking into account the nature of this railway and taking into account what was known about the economy at that point, I think the judgment that this was not only a profitable offer but a deliverable offer was made carefully and reasonably in those circumstances.

Q2 Chair: I am going to come back at you; I accept that we are being slightly wise after the event, but this was a franchise that had already failed once, so it is very difficult to understand, from our Report, what regard you had to that and therefore why, in my view, you did not do better due diligence on National Express to assess whether or not they were up to running this particular franchise.

Lin Homer: Yes. I think the reasons the franchise failed when GNER were in position and the reasons the franchise failed with National Express are quite different. I think in your Report you outline the fact that the circumstances varied between the two. In the first case, the franchise went into what turned out to be a short period of difficulty, but it occurred at a point where the holding company was financially not able to provide a degree of support. Sea Containers was at that stage in the American equivalent of administration and, therefore, there was not an option for the parent company to weather a period of lack of profitability, whereas, in relation to the National Express franchise, there was a view by the holding company that they did not want to continue managing losses over a period.

Q3 Chair: I think you are missing the point that, at the point at which the contract was signed by the Department, had you done greater due diligence, in the context of a line that obviously has some questionable profitability around the nature of the passenger population, you might, at that point, have said, "Actually, these guys are doing a lot. They are borrowing a lot. Their debt was high. Are we being greedy?" Now, I accept it is a wise-after-the-event assessment, but when I look at it I think I would have been much, much tougher at the due diligence point, and I would have taken a much stronger view on the extent of their indebtedness and, therefore, their capability of doing £1.4 billion. The thing that struck me most in our Report was figure 5. Is that the one I bang on and on about? Is it figure 5?

Geraldine Baker: It is.

Chair: What page is it?
Geraldine Baker: Sorry, it is figure 5—
Lin Homer: It is page 20.
Chair: Page 20, and you see, from the word go, they never met any of their projections. So, something leaves me thinking, "What on earth were we doing signing this contract at this level with these guys?"—their level of indebtedness, their failure right from the word go to meet the projections, and this may have been different circumstances but our knowledge that this was a line where we had already had a failure.
Lin Homer: I think there is a very appropriate challenge from the NAO and from you overall about whether, as we go forward, we stress-test differently and against different scenarios. I think that the judgments made at the time were tested against deliverability, and your point about the level of indebtedness was dealt with by both the size of the performance bond that was taken and by the requirement of a subordinated loan. So, certainly, judgments were made about the level of indebtedness that the company was seeking to carry.
I think it is possible, with hindsight, to say that we could and should have tested against a less successful outcome of the general economic position, but I think most of the Committee and most observers will be aware that, at that stage, it was not generally predicted, and your suggestion that we might in future require bidders to test themselves against a much more severe economic downturn is something I think we need to give thought to. The difficulty that you have got and the balance you have got to strike here is, if you do mitigate against what seem to be unlikely circumstances, by the nature of this process you are going to limit the commercial advantage of testing it competitively, so I think we do feel we have got to take your challenge seriously about looking at our stress-testing, but I think we made a reasonably sound assessment of what they were doing at the time. And I think you are right: there is a degree to which you can always use hindsight to look backwards, but I think the provisions put in place were reasonable in the circumstances.

Q4 Austin Mitchell: I just want to question this point about the reasons why GNER gave up the contract, because I was at a meeting in this very room, actually, between GNER, Grand Central, Hull Trains and the Department, in which the chairman of GNER made it absolutely clear that—and I do not know what the contracts are for the independent operators—if these independent operators were allowed to cut into his business, he would be out of the contract. Now, that indicates to me that there was more to it than the failure of the holding company to fulfil its obligations, which was obviously going on, and that the company itself wanted out because of the other operators that had been allowed in.
Lin Homer: I think the question of open access to any major franchise is always one that has got to be taken into account. Again, I believe that what we are seeking to do is to get the commercial firms to make the judgment themselves about the impact of those issues.

Q5 Austin Mitchell: Yes, but he was arguing that he had been sold a pup, because open access had not been in the air at that time and it was going to take a slice of his profits. The same thing was going to operate with the new operator, wasn't it?
Lin Homer: I obviously was not at the hearing that you were at, so I do not want to put words into the mouth of the company that was here, but my understanding is that, after they moved into a management contract, the GNER contract ran profitably for the remainder of the period, until we retendered it. That would tend to suggest we did not sell them a pup and that, indeed, they made a good fist of delivering what they said they would, against a backdrop of the issue of the holding company's financial support being resolved through the termination.

Q6 Austin Mitchell: You had regular meetings—I think it was monthly meetings—with the operator.
Lin Homer: Monthly meetings, yes.

Q7 Austin Mitchell: At which, presumably, alarm bells began to ring as the recession impacted on the revenue. Did these monthly meetings consider the financial health and position of the holding company as well? It was crippled by about £1 billion of debt, wasn't it, as a result of the recession and other activities?
Lin Homer: Sorry, are you talking about Sea Containers now or National Express?
Austin Mitchell: National Express.
Lin Homer: Certainly, the monthly meetings do look at a whole range of information: financial information—

Q8 Austin Mitchell: Do they look at the holding company too?
Lin Homer: They do look at the holding company, but I think one of the lessons we learned following your earlier Reports into franchises was that we should do wider analysis, and I think one of the lessons we have learned in the work we have done since this termination is that more work should have been done at an early stage about all the franchises a group holds and about the holding company position. So, I think we would accept that is a lesson learned that we can do more on in the future.

Q9 Mrs McGuire: National Express are quite a good operator in other fields in their other franchises—is that correct?
Lin Homer: I think the Secretary of State at the time said, "You are good at running railways, but you need to be able to run them and run them profitably," and certainly we expressed a view at the stage of taking this decision that we were not taking a view about their ability to stay in this business long term.

Q10 Mrs McGuire: Does that therefore lead you to conclude that there perhaps is something inherently unsustainable about the East Coast Main Line franchise, given that this is the second operator that has failed to be able to work with it?
Lin Homer: No, it does not.

Q11 Mrs McGuire: Why not?
Lin Homer: Because, first of all, as I say, there have been periods when this franchise has run well. Secondly, at the time we were negotiating with National Express what should happen in the future, National Express's view was that it was the economic downturn that had altered the circumstances, and I believe they had a view that others would follow, and that has not been the case. So, I think there is a question about the level of risk a bidder will take. That has to be a commercial decision on their part. They are balancing winning against potentially over-offering, and my view is that there is a reasonable chance of a franchisee running this well, and indeed, although there have been some challenges, we are seeing an improving performance from Elaine, particularly in recent months, which I think suggests to us that this is an area where good services can be delivered.

Q12 Mrs McGuire: I wonder, then, if Elaine would like to comment on whether or not she shares those views and what challenges you are currently facing.
Elaine Holt: I would like to comment on the revenue of this particular railway. It is quite unusual because there are not very many commuters on this route; actually, only 3% of our revenue comes from commuters and 96% is discretionary—that is people choosing to travel for business or leisure purposes, and that is very different to most other railways. There is not a stable revenue base, which makes it very difficult to forecast. I think some of the challenges for bidders, with the recession, and forecasting in those circumstances, do make it a little bit different.

Q13 Mrs McGuire: In some ways that almost makes my case. If it is so predicated on discretionary travel and you have no additional commuter travel, then surely that would lead you to conclude that perhaps the way this particular franchise has been packaged is not sustainable.
Elaine Holt: Inasmuch as it allows the commercial operator to do a really good job commercially, because it is about generating revenue, it is about advertising, it is about offering good service, so I do not reach the same conclusion, inasmuch as it is all there for the operator to make happen and it is very much within their control. I think revenue is the key line for this business for bidders and operators, and it is all about how you improve the service to deliver revenue.

Q14 Chair: So, Elaine, do you think the £1.4 billion was optimistic, if not greedy?
Elaine Holt: I do not think it was, in the circumstances. As Mrs Homer said earlier, I think the DfT made a decision based on the facts that were available.

Q15 Chair: You think it was reasonable.
Elaine Holt: I think the DfT made a fair decision at the time. I was not involved in that decision-making process, so it is really hard for me to comment.

Q16 Chair: Do you think it was reasonable?
Elaine Holt: In the circumstances, I think they made—

Q17 Chair: What circumstances?
Elaine Holt: At the time, nobody was forecasting the recession in the way that it actually came to happen, so it is very difficult to forecast revenue over a number of years in advance, and particularly predicting the recession. There were a number of bidders that bid, and the DfT did not pick the highest bidder—there was another bidder that actually offered more revenue, from what I understand.

Q18 Chair: Only just—by the end it was only just. But if it was reasonable, you are only delivering half the revenue to the Department for Transport that was supposed to be delivered under the National Express contract, and they are light by nearly £330 million to £380 million. So, you are left thinking you can only deliver half. Is that all, even post-recession?
Lin Homer: Perhaps I could answer that, Chairman. We have always expected and allowed for change in the circumstances of franchises, and we have revenue-support arrangements within all of our franchises, which do allow for changes in circumstances to be taken into account. However, within the bidding process we clearly and overtly leave the first four years of that risk with the bidders.

Q19 Chair: I understand that, but I do want to go back to Elaine Holt, if I may, because she is in charge of the company that is now delivering to us half of what they said they were going to, and we are not where we were in 2009–10.
Elaine Holt: The railway is seeing growth. In the last year—we just finished our financial year—we have delivered more than expected, so we are returning more to the taxpayer.

Q20 Chair: How much more?
Elaine Holt: It is not going to close that gap, but we delivered £170 million in premium payments. We were due to deliver a profit of £910 million and we have delivered £26 million, plus an additional £10 million in a wash-up mechanism.

Q21 Chair: Can you help on how much lower that is than was in the £1.4 billion contract? Is it half? Is it 60%? Where are we up to?
Elaine Holt: I think the best thing to do is perhaps if I do an analysis of that and provide it in a note separately. If that would be helpful, I can do that.

Q22 Chair: Okay, but can you give us some vague idea in the hearing?
Elaine Holt: I would think, at the moment, we are in the region of providing about two-thirds of the contract, but we are growing revenue and we are increasing the number of passengers travelling on East Coast, which is a good sign for the future.

Q23 Mrs McGuire: I just want to push on the sustainability of the franchise, frankly. How many other franchises have collapsed over the last three or four years?

Lin Homer: There have only been one other Section 30 terminations[1]. The GNER termination was obviously a managed contract exit, and we have not seen others collapse on the back of the economic recession. We do know that a number of them have been significantly away from the profitability they would have anticipated when they bid, and so this is an issue about what risk the company and the holding company choose to carry and what they do not. They are certainly not all where they expected to be.

Q24 Mrs McGuire: Is the Department considering whether or not this particular franchise needs to be reappraised? I think the Report, by the way, is fairly positive about the action that you took when you were faced with the action, but I think we also have to recognise that future actions will have to be considered, and given the bad luck of two franchisees having to withdraw from this particular contract, are you considering whether or not this is actually a sustainable franchise?
Lin Homer: The Department is considering overall what it should do differently around franchises.

Q25 Mrs McGuire: I want to know about this particular one.
Lin Homer: This would be included, and so there is a general view that the comments that you have made about reassessing our stress-testing should be considered; there is a general view that we should look more carefully at the financial outturn of the bid against a range of scenarios; and there is a general view that we should look at longer franchises, which obviously give companies the chance to—

Q26 Mrs McGuire: I just get the impression that Ms Holt, perhaps, does not fully buy into that analysis. I might be wrong. I am just not sure that you share that very optimistic outlook or approach.
Elaine Holt: My view of this railway is that it is often deemed by many to be the jewel in the railway crown. It is a fantastic railway delivering good service, and there are lots of opportunities for revenue. So, this is a good business that has been through some very hard times. What I can see from the DfT is they have been very keen to learn and understand the issues of the previous operators, which we have been able to share with them, and I think that will be used, from what I see, in setting the invitation to tender for the new franchisee.
Mrs McGuire: But jewels sometimes need an infrastructure to help them glow, and I am just wondering whether or not the infrastructure to help the jewel in the crown sparkle is actually there—that is what I am saying.

Q27 James Wharton: Firstly, I think it should be acknowledged that it is, as far as National Audit Office Reports go, pretty positive and complimentary to the Department, and highlights a number of things that they have found that appear to have been got right, including taking a stronger line with commercial partners when talking about a contract. We have discussed this line being the jewel in the crown. It is, in fact, the line that I quite often use to go back up to my constituency, so it would be. However, I am quite concerned by what actually happened when the termination of the contract was brought about, and the process that went on there. I understand, in summary, that National Express came forward and said, "This particular line is not working for us; it is not profitable"—for the reasons we have partly discussed—"and we would like to, effectively, buy our way out of it," and the Department's reaction to that was, "Actually, you cannot, because if we allow you to buy your way out of one line and not your other franchises, other people might do the same."
An assessment was made of the risk that that could potentially bring in terms of cost to the Department, and, in the end, instead the Department terminated this one particular franchise. Had the Department settled, it would have been about £29 million better off than with what it ultimately did, which was the termination, but the justification for that has been that that stops other rail operators from trying to negotiate their way out. That is all fine, up until I read that, in December 2010, the Department came out and said that there would be no penalty to National Express. When they bid for future franchises, you won't say, "You failed on East Coast and that is going to be held against you." Bearing that in mind, why would any rail operator now try to buy their way out of a contract when they know that, if it is terminated, there is no penalty?
Lin Homer: Gosh, that is quite a complicated set of questions.

Q28 James Wharton: It is a complex question, but ultimately it is the process of termination. What I am saying essentially is, I think you got a bad deal.
Lin Homer: Understood, yes. Could I just say it is a golden rule that permanent secretaries cannot say, "I was not there," when there are criticisms. I do think, when there is praise, I should say that, of course, this good work was done before my arrival and it is my staff who deserve the praise, so I hope you will allow me that breach of protocol. I think, in relation to the termination, as the Report by the NAO makes plain, we had to try to balance out not only the direct costs of the National Express termination, but the likely or possible impact of the decisions we took in relation to this in relation to other franchises, and, at the time, we anticipated that as many as five other franchises may be having difficulties.
I think, on page 23 of the Report, in figure 6, the NAO does a pretty good summary of the comparisons of the options, but they have done some work with us in trying to cost out those options, and if you take into account the risk of other contracts as well as the direct risk, then renegotiating the contract with National Express could potentially have cost £420 million, because you could have seen more than £300 million other costs roll in by other franchises. One has to set that against a possibility of about £250 million, so we think that this was cost-effective.
I do accept that those are a series of judgments. What I will say is, despite those five being in difficulties, no other franchisee moved into the same territory. One of

[1] GNER has been the only termination on this route. The other termination referred to was Connex South Central in 2003

the things I think we have to ensure is that we are not rewarding failure. We were very clear that there was real moral hazard in rewarding that behaviour by allowing a consensual exit—which is better for reputation, better for general market performance—when there are other franchises that are in profit, and when the reason you are exiting is because you do not want to carry the loss.

Q29 James Wharton: Absolutely, and that is helpful and sets out why the Department made the decision at the time. But to then come out and say, in December 2010, that there is no penalty for having terminated it, which means that termination was a more cost-effective option from the operator's point of view than buying out of the contract, because there is no downside to the termination route having been taken now, does that not set a dangerous precedent and send a dangerous signal to other operators that, if you terminate rather than buying your way out—if you just completely fail and the Department terminates your contract rather than you paying something—you get away with it because there is no long-term penalty?
Lin Homer: I understand. I think, on page 27, paragraph 2.35, the NAO was clear that, at their estimation, this approach cost National Express £120 million.

Q30 Chair: But—and we sometimes differ from the NAO a little bit on this Committee—on this one there was a point at which the Department was negotiating with National Express. You said to them, "£200 million and get out of all three." They counter-offered and said, "Get out of this one, £150 million," and we ended up with them getting out of this one at £120 million and hanging on to the two profitable ones, and being told that, when another one comes up, they can go for it. Accepting the whole of the NAO Report and the fact that there was more decisive action than there might have been elsewhere across Government, that does not feel like a great deal. That is really what this Committee feels. In our discussion before you came in, that was a quite strong feeling.
Lin Homer: Chair, I understand that feeling, and as you said earlier, there is always the problem of looking backwards and wondering, in negotiations, about the absolute weight of advantage to be gained. I think that does exclude the impact on their overall performance as a company by defaulting on a contract that has real trading impact on the value of their shares.

Q31 Chair: Have their shares gone down?
Lin Homer: They anticipated an impact by consensual exit and an impact by default that was different, and I just would say, again, that we also have seen that this is not seen as an attractive route. We have not seen others who are really feeling a price on their profit lines because of the economy, but we have seen them choosing to weather those difficulties rather than to take this approach.

Q32 James Wharton: I want to give you an opportunity now, because I think there is a danger that other operators will look at this as a precedent and say, "If you terminate, you get away with it." So, what was it that is special about National Express that made you say, "We are not going to hold this against you"? What was it about the way they terminated or the way they behaved when it happened, or whatever it might be, that makes this not a precedent so that other operators can look at it and say, "We can get away with that as well"?
Lin Homer: I think it goes to the conversation that has kind of moved from side to side. We were in a position where this franchisee was part of a group that was carrying three franchises at the time. They have run the other two profitably since that period. They have turned profits in relation to both East Anglia and C2C. We know they know how to run a railway. We believe the punishment that they deserved was to terminate the contract that they were not prepared to carry the loss on.
Chair: That just does not sound right to us. It just does not sound right.

Q33 Matthew Hancock: You have set out the moral hazard problem, and I think you have set it out very clearly, and you set that out in terms of not allowing them to buy their way out of the one contract, but then exactly the same moral hazard argument then applies to the default. So, could you explain why the moral hazard argument applies in the first instance, when you rejected their proposal, but then does not apply when they defaulted and the cost to them was only £120 million?
Lin Homer: I think the difficulty you have is that you are asking me to anticipate what deal we might strike with what evaluation we might take about any bid they put in in the future, and we have taken a view that we would—

Q34 Matthew Hancock: No, I am concerned that there is moral hazard around default—in trains as in every other area of life. You were very concerned, as you have just set out, about the moral hazard around allowing the company to come out of one its contracts, because you argued that you should look at the future impact on contracts as well as on the value for money in the instance, and I agree with that and I think the whole Committee would. But then we came to the default, and precisely the same argument applies in terms of the consequences of the default, especially if you do not put constraints on a company following default, because the incentives to default and use the default route rather than do anything else mean that moral hazard applies just as strongly there.
Lin Homer: Yes, but one of the things that we have sought to do, from your Reports and from our own experience, is to learn lessons from the past and take them into the future. So, in relation to this contract, we had both a subordinated loan and a performance bond, and we had moved into that territory because previous experience had shown that, if you do not have mechanisms that tie holding companies in, you can be left exposed. Now, we have not suggested to National Express that there won't be lessons to learn about this.

Q35 Matthew Hancock: But lessons to learn is different from cash to pay.
Lin Homer: Going forward with new franchises, our expectation of what obligations we will place on holding companies, on what financial security we have, will be improved by this experience.

Q36 Matthew Hancock: Specifically related to National Express?
Lin Homer: Well, that will apply to National Express.

Q37 Matthew Hancock: No, but will it only apply to them?
Lin Homer: No. We have to be satisfied we are in circumstances where we are confident the bid is deliverable, so we are absolutely able to look at past experience. Indeed, one of the things the Secretary of State may well more take into account is the deliverability. So, we have not ruled them out and we have made no promises that they will automatically pre-qualify.

Q38 Matthew Hancock: Then the question is this: there was a deal on the table that they were offering to pay £150 and get out of the one contract—
Lin Homer: Million. That would have been a bad deal.

Q39 Matthew Hancock: Thank you, yes. And then the outcome after your tough negotiation was that there were costs of £120 million, so you negotiated yourself out of 30 million quid.
Lin Homer: If I might say so, Chair, that is a simplified summary of what happened.

Q40 Matthew Hancock: So, it is a summary of what happened.
Lin Homer: No. I think it ignores the impact on the wider market. As I say, if you look at figure 6, if you put figures to figure 6 in the NAO's Report, I think the NAO believes, and we would concur, that we could easily have lost another £300 million by a consensual exit.

Q41 Chair: Can we get this clear: are you saying to us that the reason we—the taxpayer—lost £30 million—
Lin Homer: I do not believe we accept that we did lose £30 million.

Q42 Matthew Hancock: But you accepted the £150 million and the £120 million. Is the difference between £150 million and £120 million £30 million?
Lin Homer: No, that is the point where I am arguing that you are being a little bit simplified.

Q43 James Wharton: The reason we lost that £30 million.
Lin Homer: Yes. Because if we had shown we were prepared to do deals at that point, we believe we would have had a number of other franchisees lining up—

Q44 Matthew Hancock: But you did a deal at £120 million.
Lin Homer: No, we did not, we did not. We terminated by a default event and we claimed all that we were contractually entitled to.

Q45 Matthew Hancock: Yes, and what was the cost to the company?
Lin Homer: So, in the future, if that figure is higher, then the penalty will be higher. So, we were taking a macro look at this, not an individual one, and that is where I think I am differing—

Q46 Matthew Hancock: So, instead of a deal with a fixed figure, it was a default based on the principal, which, in this case, was lower.
Lin Homer: It was £120 million but in future might be more.
Amyas Morse: Were there any limitations to your legal position that meant that you could not claim more?
Lin Homer: Those were the extent of the arrangements that we had entered into in relation to this contract. So, that is the part where, going forward, we can learn some lessons.

Q47 Stephen Barclay: Where Amyas is going is where I wanted to go. By enforcing the contract, as I understand it, and enforcing your legal provision to terminate, you recouped £120 million.
Lin Homer: Yes.

Q48 Stephen Barclay: But what seems unclear to me in the NAO's Report is whether, legally, you had the option of terminating those two franchises, because paragraph 15 says, "The Department may terminate any other franchise owned by a holding company," and then at paragraph 2.19 on page 23, it said, "In these circumstances," talking about East Anglia and C2C, "the Department did not have clear grounds to force a return of the other two franchises." So, could you clarify legally whether it was the Department's view that you could terminate the other two franchises?
Lin Homer: No. I think, at the time, there was a view that we could not find triggers or events that would lead to default in the other two. However, one of the recommendations from the Report is that we do a lessons learned, and one of the lessons we believe we could learn from this procedure is that we should—

Q49 Stephen Barclay: So, it was the Department's legal view at the time that you did not have the legal powers to terminate the other two franchises.
Lin Homer: Yes. But at that point, under our arrangements then, we had a franchise lead manager for each franchise, and one of the lessons we believe that we should learn from this is, at the point that we go into difficulties—and again I think you are right; we began to have concerns about this franchise from seven or eight months in—there is a view that a lesson learned should be that we bring all the leaders of the franchises, in a single group, more into the fold and we monitor different events more carefully.

Q50 Stephen Barclay: Sure. So, building on that, and there are always learned, I would just point out

that Nick Olley, who is a partner at Burges Salmon, was quoted in *The Guardian* in July 2009—which the Chair knows is a paper I read assiduously—as an expert on complex rail contracts, saying, "Termination as a result of an event of default of any other franchise agreement to which the franchisee or an affiliate of the franchisee is a party"—he goes on to say that is grounds for terminating the other franchises. So, what you are saying is, firstly, his legal advice as quoted was not the view of the Department.
Lin Homer: It is certainly a possibility, but I think the thing that we were not doing at that stage was necessarily casting our eyes over the whole range of behaviour over all three franchises assiduously for events of default. I do not think it is automatic.

Q51 Stephen Barclay: You were suggesting a moment ago that the Department's legal advice was that you could not terminate the other two; now you are saying it was a possibility.
Lin Homer: No. I do not think we could automatically.

Q52 Stephen Barclay: I assume the Department took QC's legal advice on this.
Lin Homer: We had a range of advice from experts, and at the time they did not think there were grounds to terminate the other two. One of our lessons learned is we think that we need to look for default events assiduously across the whole group in future events. We may have been too much in separate silos on this occasion.

Q53 Stephen Barclay: Sure. So, if you did not have the legal power to default the other two contracts, what was the maximum exposure of this stand-alone company on a £1.4 billion contract?
Lin Homer: It depends on the point at which they defaulted, but at the point that they did—
Stephen Barclay: At the time of default.
Lin Homer:—we had a right to a performance bond and we had a right to a subordinated loan.

Q54 Stephen Barclay: No. What was the maximum exposure when they defaulted? You entered into a legal agreement with a stand-alone company on a £1.4 billion contract. What was their maximum exposure?
Lin Homer: We think that the £120 million was the exposure at that point.

Q55 Stephen Barclay: And that is an adequate termination provision within the contract?
Lin Homer: It depends on the point in the contract, and you will be aware that this was a payment profile where much of the premium built up as the contract went on.

Q56 Stephen Barclay: Since the point at which you terminated that contract, what additional revenue support have you given on the other two franchises to the company concerned, and does that outweigh the £120 million they paid for getting out of this unprofitable contract?
Lin Homer: I am afraid I could not quote you the revenue support absolutely off the top of my head for the other two, but it will not be in that order.

Q57 Chair: Can you let us have a note within a week on that?
Lin Homer: Yes, of course.

Q58 Stephen Barclay: I think I quoted a figure of massive increased profits over the last 18 months on those other two franchises. I think 544% was the figure, but I may be wrong on that. I am sure people can check.
Lin Homer: The profits on East Anglia are around £15 million for last year, and on C2C around £4 million, so even if one took a view that all of that was revenue support, which is unlikely, then that is what suggests to me that you are not in that order of things.

Q59 Stephen Barclay: Sure, but they have been able to extend those franchises, so the profit has gone on for further.
Lin Homer: The reason that we took the tough line that we did is we did not think that one company should be able to profit from ditching the unprofitable one with no loss of market reputation, no consequences, whilst they kept the other two. That was a big part of the decision making.

Q60 Joseph Johnson: I just want to go back to the point Stephen initially raised, which is the vagueness I detect in your answer as to whether the Department was clear about whether it had the legal right to terminate the two other contracts. Certainly, I don't really feel I got a clear answer from you, especially given that the Department, at one stage, appeared to be considering a consensual exit that was premised on a cash payment of £200 million and the surrender of all three of the company's rail franchises. If you are entering into a negotiation with that as your starting point, it suggests that you have the legal basis to go down that road, but you are now saying the Department did not have the legal basis to go down that road.
Lin Homer: We would have had a legal basis to do that consensually, because it was by consensus, so the offer from National Express to negotiate an exit, as far as we were concerned, should be punitive and should cover all three. I am sorry; I did not mean to sound vague. From my review of the work that was done at the time, it is clear to me consideration was given as to whether we should default all three. I don't think there was a clear event of default in the others, and I think that was why the decision was taken that we did not trigger default.

Q61 Chair: Just for the record, can I make clear: the Department at the time did not pursue whether or not you could terminate the three. The Department, in some way, took a decision to focus on just this franchise and not bring in the other two. So, it was not that there was legal advice saying you could not; it was a departmental policy decision not to look at the other two.

Lin Homer: No, Chairman. There are pages and pages of consideration of the position. As your report makes plain, throughout there were really three options: one was to renegotiate the whole contract; one was to have a consensual exit; and the other was to terminate. Against all three of those options, considerable work was done on both the financials and the legals. I am not saying we did not consider; what I am saying is, on the facts that were available at the time, we did not believe we had grounds to terminate the other two. However, a lesson that we believe we should learn from this is that we did not involve all three franchise managers from the earliest point when we had concerns about this one, and it may therefore be that, if we had been looking in a more collaborative, more coordinated way, that we would have reached—

Q62 Chair: So, you did not test it legally?
Lin Homer: We think we could and should test more fully in the future when there is more than one franchise owned by one group. That is different from suggesting we did not consider it, I think.

Q63 Joseph Johnson: Essentially, would you agree that National Express had an unlimited upside if things went well and the sky's the limit in terms of everything going well, the economy continuing to perform as if there would never be another recession ever again, as the Bank of England and Oxford Economics forecast; on the other hand, it had a basically very cheap put on the taxpayer in the event that a recession duly came along, as they tend to every seven or eight years?
Lin Homer: No, the upside is not unlimited. There is a revenue-sharing arrangement that kicks in once you are at 102% of anticipated revenue. Initially, the taxpayer gets 50% of the extra revenue, and then 80%, so the upside risk is also shared. It has been the case in the last few years that we have been doing more sharing of downside risk—I am absolutely clear about that—but for both circumstances being better than when bid and being worse, there is a risk-sharing arrangement, and we are again looking at whether there are different and better risk-sharing arrangements for future franchises.

Q64 Chair: Can you tell me how much you spent on consultants to support you during this period?
Lin Homer: Overall, we spent £15 million to terminate the contract and bring DOR into effect, which is about half of the £31 million performance bond. The bond exists to at least cover those arrangements.

Q65 Chair: Is that the total bill? It is just that your Department, as you know, has a reputation for generous use of consultants, and I am just interested in this one as to how much was spent on the whole issue of considering what to do over the future of the National Express contract, bringing it to an end and then negotiating with Elaine Holt—the whole saga.
Lin Homer: That is the total.

Q66 Chair: £15 million is the total, and that is not including staff costs?
Lin Homer: No. That includes additional direct costs.

Q67 Chair: But not your in-house staff.
Lin Homer: Could I write to you, Chair, to let you know about that?

Q68 Chair: You can write to us on that. The other thing that might be helpful is also to get a feel from your Department, because it is one of the things we are monitoring, of how many people in the Department worked on this.
Lin Homer: Yes. There will have been a significant number over time, initially standing up the off-the-shelf companies and then bringing in experts.
Chair: If we can have a note that sets out the number of in-house staff and the expenditure on consultancy throughout this period, I think it would be helpful.

Q69 James Wharton: Ms Holt, did you say that you made a profit of £26 million this year?
Elaine Holt: Yes.

Q70 James Wharton: Again, the figures for the other two franchises National Express were using were £15 million and £4 million, so about £19 million, so it really is quite a profitable line that we are talking about here, isn't it, or it should be?
Elaine Holt: Yes.

Q71 James Wharton: That makes it all the more significant, I think, that we have had two Section 30 failures on this route[2]. Really, it is a question for the Department: you are going to retender this in 2012. What have you learned and what are you going to do to make sure that this does not happen again?
Lin Homer: I think we will need to ensure we have learned the specific lessons about East Coast and that we, in addition, are applying the wider range of reviews that we are looking at for franchises generally. The Secretary of State has a view that we should let longer franchises. We are interested in looking at the advice you have given us about stress-testing. We do believe that we should look at the degree to which previous performance is taken into account—actual deliverability rather than the proposition that is on the paper. We obviously have to take into account how much we stress-test bids against unexpected but possible financial scenarios, although, as I said earlier, that is quite a complex one because you could end up reducing the entrepreneurial innovation you allow if you always go back to saying, "Yes, but cost in a recession around every corner." So, I think we will be very determined to learn all of those lessons.
I think all I would say is that, in overall terms, the Department has let 47 franchises and two have had Section 30 terminations, so that does suggest that the gradual learning that the Department has done, absolutely with support and help from your Committee and from the NAO, has created a reasonably strong base for franchises, and we want to build on that as we go forward.

[2] There has only been one. The GNER failure was a managed exit.

Q72 James Wharton: I think I would accept that, and there is quite a useful summary there of some of the broader issues that you have learned, but you said you will need to learn the specific lessons for East Coast as well. What are they? You have had two failures; they have both been on this line. It should be a profitable line. Something has gone wrong. You have mentioned a number of broad lessons that you have learned, which is great. What are the specific lessons that you have learned on this line?
Lin Homer: I think what we have to do is stress-test a financial bid in relation to a line that is dependent on business and leisure trade rather than commuter trade. I think one also has to say that the detailed plans that are put in need to be looked at. National Express did put into place both cost-cutting and business-generating activity during the first year, but, as the Chairman has pointed out, they were off-plan from quite early on, so it is also a question about testing the deliverability of the specific plans that are put in when there is not an underlying commuter business as a cushion against the undertakings of the individual company.

Q73 James Wharton: Both of those examples have drawn back to the nature of this line not having an underlying commuter business. Are you saying that that is the key reason for these two Section 30 failures? There seems to be a thread that runs through them. The specific lessons that you have learned both link back to that. Do you think that is the key factor?
Lin Homer: No, I do not wholly, because I think this is not the only long-distance route that is heavily dependent on business and leisure.

Q74 Chair: I was going to say, the other one up the other side, whatever we call it—
Stella Creasy: The West Coast.
Chair: The Birmingham one.
Lin Homer: West Coast?

Q75 Chair: Yes. That is the same, isn't it?
Lin Homer: That is exactly the point I was seeking to make. What we have got, I think, is a really difficult and challenging period for the East Coast line. I do not want to deny that at all. One of you mentioned infrastructure but we moved on too quickly for me to respond to that. There are infrastructure requirements on East Coast. The introduction of the new intercity express trains may well have the same kind of significant impact the Pendolinos have had on the West Coast. So, I do not for a moment suggest there are not lessons to be learned. I do not think we believe long-distance intercity travel is innately unprofitable or difficult. What we have got to do is get the balance right for East Coast next time.

Q76 Stephen Barclay: Could you just clarify how you will get passenger forecasting right? On this franchise, you hugely overestimated the numbers, and I think, on the Great Western, you have hugely underestimated the passenger numbers. You are now looking to have much longer franchises. I am just wondering how you are going to alleviate that problem.
Lin Homer: The question about how we forecast obviously has to take into account what we already know about patterns of behaviour, but the shape of the franchise will obviously also impact on that, because it is a question of where the risk lies. What I think we are looking to get into in the future is, in a way, less second-guessing of the commercial operators and more freedom for them to arrange the franchise in such a way that those things are more at their risk.
There might then be a need, as you suggested to us, when you look at the revenue support arrangements to move to something that is a different form of protection than our current cap and collar, but I think we believe that we have got to try to move away from is the idea that we can, at a point in time, make a single forecast on which we base a single premium and then that is it, to an arrangement where commercial risk is transferred and there is taxpayer protection for the upside of that, some company protection if things like a big economic recession impacts, but where that balance of risk is fair between the taxpayer and the company.

Q77 Chair: It is quite interesting that the McNulty interim report has said that the franchising in Germany and Sweden has led to a cost reduction of 20% to 40%. Here, if you look at our train-operating costs since 1996–97, they have gone up by nearly 20%. Partly, I understand, that is engineering costs, but I am told that, according to McNulty, it is also procurement strategies and asset management. What confidence can we have that you know what you are doing as you move forward in getting value for money out of the future franchises?
Lin Homer: Yes. The interim report from McNulty suggested that we are between 34% and 40% more expensive than Europe. I think part of the confidence is that the Secretary of State intends to adopt a new approach to franchising based on the McNulty review and based on contributions from the sector. There is a question about moving away from an approach that can be seen as having too comforting a revenue-protection system, so that, as I say, it absolutely transfers the risk for the first four years, but then one moves into revenue protection. There is then a kind of jeopardy about that, because, coming out of revenue protection is almost like the benefit trap for TOCs, isn't it? We are looking at whether we can find a mechanism that puts back more opportunity for commercial creativity and more opportunity for commercial freedom. That is absolutely something that the Secretary of State will be looking to take forward in the rail reform that will follow on from McNulty.

Q78 Chair: Moving to 22-year contracts?
Lin Homer: Moving from our current seven contracts to longer contracts, partly because the feedback from the industry is that there is not a long enough period of investment to make—

Q79 Chair: How are you going to ensure value for money for us?
Lin Homer: That is part of what the Secretary of State is going to have to look at as we go forward. It is

why we think that different forms of stress-testing and different forms of protection will be necessary, but there is always a question here about allowing the taxpayer to gain advantage from commercial involvement in the business versus protecting the passenger, because we will always be the operator of last resort. The balance between those two things has to be fairly carefully weighed. Get it wrong, the passenger suffers, but go too far the other way and, although the passenger is protected, the taxpayer pays too heavy a price.

Q80 Chair: We have got quite a way to go to catch up with our European—
Lin Homer: I believe we have and I think we are very determined to try to narrow that gap.

Q81 Chair: You would know the three or four things you have got to do differently, do you?
Lin Homer: I think we believe we are in the right territory, in that the intention for the discussions we have between now and November, when the Secretary of State is committed to publishing plans, is that those are based not only on the McNulty review but on what the industry believes it is capable of doing and the best practice we can learn from other parts of Europe, as well as ourselves.

Q82 Chair: What would you say? Have you any idea? Am I asking you too early on? What sort of things?
Lin Homer: No. I think Roy McNulty has given some indications in—

Q83 Chair: What?
Lin Homer: Well, length of franchises, a focus on value for money.

Q84 Chair: Yes, but how do you get the value for money?
Lin Homer: Closer alignment of the incentives so that we do not have a system where it is in the interests of the train-operating companies and the infrastructure provider, in a sense, to play off against each other; potentially looking at the degree to which we can change the revenue support arrangements, so that, as I described it, this risk of dropping into a revenue support trap can be alleviated. I think we think there is a range of ways that we can get a better deal for the taxpayer while still giving the passenger the services that are needed.

Q85 Chair: So, is it a mistake to have the regulation and monitoring of the regulators separate from the regulation and monitoring of the operators?
Lin Homer: It is something, I think, you are going to be looking at on Wednesday, isn't it, and I have no doubt, when you have me back, that we will talk about that. So, it is certainly an area that we will be interested in your views on, Chair.

Q86 Austin Mitchell: Since it is working very successfully now, and there are a few more delays but they are mainly due to Network Rail rather than the company, why not just keep it as a nationalised entity—a jewel in the crown of the Department for Transport and a comparator and example to the rest of the system? Why not keep it nationalised?
Lin Homer: We have to compete the railway under the arrangements by which we run the system. You are absolutely right, and I am sure Elaine will speak to it herself, but we do believe that the operating performance overall—and particularly in the last couple of months—is improving, but it is important that we show that we have tested that.

Q87 Chair: You can change. If we have got something that is working, if it ain't broke, why fix it?
Lin Homer: I think a number of Governments over time have believed that, in the main, the commercial running of the railways should be in the private sector.

Q88 Austin Mitchell: Are you saying that you don't want to keep it nationalised, or the Government won't let you keep it nationalised?
Lin Homer: We couldn't under the current arrangements. You would have to have legislative change. I think we believe that competition in the railways is one of the ways that you can bear down on the cost to the taxpayer.

Q89 Chair: Are you going to compete?
Elaine Holt: As East Coast? No, we are not going to.

Q90 Chair: Because?
Elaine Holt: We have looked at it and we believe that our focus is on turning round the business and delivering excellent performance, and to compete would be very distracting for the East Coast team.

Q91 Chair: So, you are waiting for the next one to go down, are you?
Elaine Holt: I could not possibly say that.

Q92 Austin Mitchell: The paint shops and the uniform providers are doing very well out of the East Coast franchise, aren't they? They keep changing the paint, keep changing the uniforms, keep changing the rolling stock, yet, as a nationalised entity, you could just keep the identity that you have got.
Elaine Holt: The fleet colours are changing from blue to silver, and that is part of an overhaul that happens every few years and, as part of that overhaul, they get the rust treated and the fleet repainted, so that is no additional cost—it is just something that is happening, and it is happening very slowly. You see our trains in lots of different colours.

Q93 Stella Creasy: Would you like the legislation to change to be able to compete?
Elaine Holt: I think the reality is that bidding is a very serious business. It takes a lot of resources, and for East Coast to bid we would need a partner. I think, in the current climate, the right decision for this particular railway is to focus on doing the day job, getting it right, and then working very openly with the bidders to make sure that we give as much information to the bidders coming in to then carry on the good work that we are doing.

Q94 Stella Creasy: Do you think you have got enough time in the time left to do that, or do you think that the deadline for the franchise to be renegotiated should be put back to allow you the time to do that?
Elaine Holt: We have got another 18 months to deliver. Our plans are geared up to that. We are making lots of investments that will not only bear benefits now but into the next franchise term. So, we are aware of the date, we are working to it and we are happy to continue it as long as the DfT want us to do that.

Q95 Stella Creasy: So, you are doing the line up, you are improving its performance, you are improving the rolling stock, and you are going to walk away and it is going to be retendered.
Elaine Holt: Yes.

Q96 Stella Creasy: What are the risks to the taxpayer? It is taxpayer money that you are spending doing all this work, so we are investing in it now but we do not necessarily get the opportunity to continue that good work, do we?
Elaine Holt: A lot of the investments that are being made at the moment are for longer term benefit. So, some of the changes we are making deliver payback over four or five years, and the taxpayer will get the benefit when it is re-let in the sale process or whatever it is to be going forward, so the taxpayer will get value back from it.
Stella Creasy: But to National Express it will look very attractive.

Q97 Austin Mitchell: Make it successful for these two years and then show the bastards. I have one parochial question: the map, page 15, shows a spur from the East Coast main line going to Lincoln.
Elaine Holt: Yes.
Austin Mitchell: Why doesn't that go on to Cleethorpes, and what are you going to do with the trains overnight?
Elaine Holt: I think we have talked about that when we met, so I think the opportunity is that the DfT are currently looking at the specification for the new franchise, and I think Cleethorpes and various other places are all keen to have East Coast run trains there, and that is an opportunity we will look at with the DfT.

Q98 Austin Mitchell: When you go out to the bidders, are you going to impose a requirement that they go to Cleethorpes?
Elaine Holt: That is for the DfT to consider.
Lin Homer: We are looking with franchisees at giving them the scope to think about services and, in a sense, seeking to be less regulatory about what stops and where, and to allow them to develop services. So, I think you are going to have to wait, I am afraid, Mr Mitchell, for the franchise.
Matthew Hancock: Could you do one to Haverhill as well? You would have to build the track first.

Q99 Austin Mitchell: Cleethorpes comes first—it is more bracing. Where will the train reside overnight if it stops at Lincoln? You cannot keep it at Lincoln—it has got no facilities. You could keep it overnight in Cleethorpes.
Lin Homer: I sense a number of bids coming out of the Committee, Chair.
Chair: Actually, I thought James would bid for a restaurant car.
James Wharton: I want the restaurant car back.

Q100 Chair: He says you have closed the restaurant car. Why have you done that?
Elaine Holt: During the recession, last year we saw £37 million of revenue lost to people downgrading from first class to standard, so what we are trying to do is make the first class product much more attractive and we are going to be offering, from 22 May, an inclusive meal in first class with your ticket.

Q101 James Wharton: I cannot afford first class.
Elaine Holt: There are some very good fares in first class.

Q102 Chair: So, what happens if you are non-first class?
Elaine Holt: We offer hot meals from the trolley bar and the buffet, but do come and try it from 22 May.
James Wharton: If only I could afford it.

Q103 Stephen Barclay: Two things, really. First, just to clarify, further to Austin's question: punctuality has actually got worse since you took over, has it?
Elaine Holt: Yes, it has.

Q104 Stephen Barclay: And the reason for that is? Notwithstanding Network Rail, but your own part of it in terms of your own efforts has actually got worse.
Elaine Holt: Absolutely. The public performance measure has deteriorated year on year. I think you can see from the Report there are three causes of delay. 63% of the delays are caused by Network Rail. At the time of the Report, we were 25% of the delays. That has reduced to 21%. For our own causes, it is predominantly around the fleet. It is an ageing fleet that perhaps, over the years, has not had the tender loving care it needed and, in the last 18 months, we have been putting that right. In fact, in period 13 this year, we saw the lowest ever TOC-on-self delay for this railway on record, which is 11 years. So, for East Coast, we are really starting to turn things around.
I did actually ask Network Rail what they would say if they were here today about their performance, and they have said that they recognise it is not good for the East Coast main line, and particularly East Coast itself, but they have actually said it is improving and it is the top priority for their board. I think they understand they have got to do a lot, and I think East Coast can demonstrate progress and we are going to continue to work hard to improve it further.

Q105 Stephen Barclay: Just coming back to Ms Homer's answer to the question about passenger forecasting, I did not really follow practically how that is going to impact. If one looks at, for example, High Speed 2 and the impact on other lines, are you saying, on very long franchises, you are going to have breaks in the agreement and that you are going to have discretions for the Department to change the commercial terms in significant ways? How, operationally, is that going to happen?

Lin Homer: We have not completely finalised how we should franchise for the future, so this is all an area for debate, but there are a number of aspects about the number of passengers. More passengers may be good for revenue but, if you get to the point that West Coast has, where not all the passengers who want to can either get on a train or get a seat, then you can reach a point where the level of crowding becomes unsatisfactory. So, there are issues about overall capacity that need to be looked at, and the incentives to encourage operators and infrastructure providers to increase capacity—it may be rail capacity; it might be carriage capacity. There are questions about the fares that you charge and at what times to try to even out when people use the trains. Again, looking at us and Europe, overall, although our trains are very busy sometimes, they are not as smoothly busy as other places in Europe, and so we want to see what we can learn about that.

There is a question about increasing capacity. We have done so remarkably over the last few years, and the capacity on the railways overall has gone up enormously since the early 2000s, whether you look at passenger miles or you look at journeys. There were a billion journeys back in 2002/03, and there are now 1.25 billion. There were 40 billion passengers then, and 51 billion now. Those are enormous figures, but you want them to be smoothed and filling up the trains.

Q106 Stephen Barclay: One of the things we know from the previous hearing we had is that the Department does not accurately measure journeys now; for example, it overestimates journeys from cities and underestimates journeys from rural stations. A lot of rolling stock does not scan passengers on and off, which gives inaccurate data. What I am driving at is we see, with this Report, passenger forecasting being hopelessly wrong. We have seen that elsewhere as well, sometimes too high, sometimes too low. Your own capacity to measure what the situation is now, today, is flawed. That strikes me as not a very good basis on which to do accurate passenger forecasts over very long periods, and so it then begs the question: to what extent are you building flexibility into the contract in a way that was not the case with this? We have established that, on a £1.4 billion contract, you only had a penalty clause of £120 million, which is derisory. So, to what extent are you building that flexibility into the likes of High Speed 2 in order to give the Department the levers it needs?

Lin Homer: I think we are better at forecasting than we were. There are mechanisms nowadays, as you know, for counting people as they board carriages. The belief is you do not necessarily need to have that in every carriage, but having more of that allows better forecasting. But I think what we also want to get is, in a sense, cleverer contracts that put an emphasis on the train operator to attract people to the trains that have capacity and away from the ones that are full.

Q107 Chair: We are slightly ahead of you on that one, because if you look back at our Report on overcrowding, one of the failures of the Department was not to insist that all your operating contractors used a very simple counting mechanism, and that should be part of the franchises. I think that is one of our recommendations, so we hope you are implementing that. The Treasury minute says you accepted the recommendation, so we are assuming and we will monitor that you are implementing. I just want to ask you three bits we have not covered, but very rapidly because everybody has to go: one is you have got less money in the Department—£330 million to £380 million less than you thought. What has gone?

Lin Homer: In relation to this contract, and to franchises overall, we had made provision for a level of revenue support, so we had anticipated, once the recession became evident, a level of a revenue support.

Q108 Chair: What provision did you make for that?

Lin Homer: We made sufficient provision in the spending review period.

Q109 Chair: How much?

Lin Homer: Our overall budget allowed for a number of payments to be made to revenue support.

Q110 Chair: How much?

Lin Homer: The total sum is difficult**—**

Q111 Chair: This is a heck of a lot. This is £330 million to £380 million less than you thought you were going to get.

Lin Homer: Over the period. This year we have made—

Q112 Chair: What is your provision this year for bad—

Lin Homer: This year we made more provision than turned out to be needed.

Q113 Chair: Okay. How much?

Lin Homer: The Chancellor, in the Budget, announced £85 million of additional rail infrastructure spending on the basis that we were not using all of our support spending.

Q114 Chair: How much was the support spending? I am sorry to push you—what was it?

Lin Homer: I am afraid I cannot tell you.

Q115 Chair: Will you tell us in a note?

Lin Homer: Yes. What I can tell you is that about £200 million of what we anticipated would go into revenue support went into investment in the railways, so we have not had to make cuts. We have been able to invest.

Q116 Chair: It depends—£200 million on what? It is the "what" that we would like to know.

Lin Homer: Stations, the Manchester line—

Q117 Chair: Yes, but £200 million as a percentage of what?

Lin Homer: Yes.

Q118 Chair: Then could you have dealt with more than one failure?
Elaine Holt: Yes, we could.

Q119 Chair: You could? Just finally, give us the three or four things that you are doing to grow the value of the company.
Elaine Holt: This business, as we have heard, is all about revenue, so we are investing in revenue-forecasting technology, improving on what we have got today; we are investing in the fleet to improve performance; we are investing in customer service—a whole variety of things, and all of those things will improve punctuality and customer service and drive revenue.
James Wharton: But no restaurant car.

Q120 Chair: Does your bonus depend on this revenue and his restaurant car?
Elaine Holt: East Coast is targeted on delivering £617 million revenue this year, and we aim to do that through encouraging customers to travel with us.

Q121 Chair: And your bonus is based on which performance measures?
Elaine Holt: My bonus is based on a whole variety of things, including performance, revenue, safety—clearly, very importantly—and customer service.

Q122 Chair: And you have managed to get that each year?
Elaine Holt: The business itself, in the last year, achieved a majority of its key performance indicators. It did not achieve everything but it made substantial improvements in key areas, particularly safety, so we are looking at East Coast and how we reward managers under the bonus scheme.

Q123 Chair: So, you and others got your maximum bonus.
Elaine Holt: No, no. Nobody in East Coast gets the maximum.

Q124 Stephen Barclay: What was the bonus pot?
Elaine Holt: My personal one?

Q125 Stephen Barclay: You can if you like, but the bonus pot as a whole as well.
Elaine Holt: My personal bonus is linked to the civil service, which is capped at £12,500, so it is an absolutely—

Q126 Stephen Barclay: And the bonus pot?
Elaine Holt: For East Coast itself, we employ 3,000 staff nearly, the maximum bonus pot is around £1 million, but we are not going to spend anywhere near that. It will probably be, I would think, in the region of £600,000.
Chair: Thank you very much indeed. Thank you for being so straightforward, and we won't see you tomorrow, but we will see you, I am afraid, in a couple of weeks' time. Thank you very much indeed.

Written evidence from the Department for Transport

During the evidence session 9 May 2011 I offered to provide additional information to the committee. This additional information is attached in the Annex to this letter.

I also wish to make some factual corrections to the transcript, marked in track changes in track changes in the attachment to this letter.

19 May 2011

Annex

ADDITIONAL INFORMATION FOR THE COMMITTEE

Q21 *Delivery of premia payments by East Coast in comparison to £1.4 billion NXEC contract*

From the start of the franchise until the point of termination, franchise payments were received from NXEC in line with the franchise agreement. In the financial year 2010–11 NXEC was due to pay premia payments of £303.8 million (adjusted to take account of the Office of Rail Regulation's five yearly review (Control Period 4) and in 2010–11 prices).

Projected premia payments payable by East Coast in 2010–11 are likely to be £196.7 million, representing 65% of the premia payments due to be paid by NXEC.

Q56 *Additional revenue support provided to National Express Group's two other franchises*

National Express Group manages c2c and National Express East Anglia. c2c has not become eligible for Revenue Support and is therefore not in receipt of payments. NXEA is eligible for and in receipt of Revenue Support and received approximately £40 million in year 2009–10 and £37 million in year 2010–11. These are full year figures, calculated cumulatively, as accurate mid-year figures cannot be given.

Q65–68 *DfT spending on contractors and DfT staff involvement*

The cost of the termination project, including the future anticipated costs for re-letting the franchise, is expected to total £15 million. This is made up of:

— Specialist advice and support: Approx £4.9 million.

— DfT staff costs: Approx £0.74 million.

The remainder of the balance was made up of DOR operating costs.

Twenty-five DfT staff worked either on a full or part time basis on the termination and subsequent mobilisation of East Coast.

Q114–115 *Support spending*

The Department forecasted revenue support payments totalling £205 million and £543 million for 2009–10 and 2010–11 respectively. Actual payments were higher in 2009–10 by £87 million but lower in 2010–11 by £208 million. The savings made in 2010–11 were used to invest back into the rail infrastucture.

ISBN 978-0-215-56040-7

9 780215 560407

PEFC

PEFC/16-33-622

Printed in the United Kingdom by The Stationery Office Limited
07/2011 012197 19585